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D.T.E. 99-66-A

Investigation by the Department of Telecommunications and Energy on its Own Motion Into Fitchburg Gas and Electric Light Company's Recovery of Costs Related to Gas Inventory

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TABLE OF CONTENTS

I. INTRODUCTION

On November 1, 1999, the Department of Telecommunications and Energy ("Department") initiated an investigation to determine whether Fitchburg Gas and Electric Light Company ("Fitchburg" or "the Company") overcollected costs related to gas inventory: specifically, whether the Company collected gas inventory costs both through its base rates and its Cost of Gas Adjustment Clause ("CGAC"). This matter was docketed as D.T.E. 99-66. The Notice of Investigation stated that the Department would investigate: (1) whether Fitchburg had overcollected for costs related to gas inventory; (2) the amount of any overcollection; and (3) whether Fitchburg's ratepayers are entitled to reimbursement. Fitchburg Gas and Electric Light Company, D.T.E. 99-66, Notice of Investigation at 1 (November 1, 1999).

The present investigation arises from Fitchburg's last gas base rate investigation. On May 15, 1998, Fitchburg requested its first gas base rate increase in approximately fourteen years. Fitchburg Gas and Electric Light Company, D.T.E. 98-51 (1998). In that proceeding, the Department stated that it appeared the interest on gas inventory, which was being collected through the CGAC, may also have been included in the Company's rate base. Id. at 20-21. The Department ordered Fitchburg to remove the proposed inventory finance charge ("IFC") component of the Company's materials and supplies balance from rate base. Id. at 20.[(1)] The Department also stated that we would open a separate proceeding to determine whether any overcollection of IFCs occurred. Id. at 21. In addition, the Department found that Fitchburg had not complied with 220 C.M.R. § 6.06, requiring use of a financing vehicle or trust to finance its IFCs.[(2)] Id. The Department ordered the Company either to petition the Department for approval of a financing vehicle or trust or to request an exception to the regulations pursuant to 220 C.M.R. § 6.12. Id. at 22.[(3)]

Fitchburg's prior rate case history is also material to the instant investigation. In 1983, the Department approved gas tariff schedules for Fitchburg. Fitchburg Gas and Electric Light Company, D.P.U. 1214 (1983). Under the approved rate structure, Fitchburg recovered interest on gas inventory through a materials and supplies component included in rate base. Such recovery was common industry practice at the time. See, e.g., Boston Gas Company, D.P.U. 1100, at 6-11 (1982); Lowell Gas Company, D.P.U. 19666/19677, at 14-15 (1979). Fitchburg requested a gas rate increase again in 1984. Fitchburg Gas and Electric Light Company, D.P.U. 84-145 (1984). In that latter case, the Company also proposed in its initial filing to collect interest on inventory through a return on rate base (Exhs. FGE-2, at 9; AG-1, at 12; Tr. 2, at 198-200). Ultimately, the Department approved a settlement negotiated by the Company and the Attorney General of the Commonwealth of Massachusetts ("Attorney General") that did not specifically address interest on gas inventory ("1984 Settlement") but did reduce the requested rate increase for gas operations from $1,450,983 to $816,218. D.P.U. 84-145, at 1, 3.

II. PROCEDURAL HISTORY

Pursuant to notice duly issued, the Department held a public hearing on December 8, 1999, to afford interested persons an opportunity to comment on the investigation. The Attorney General filed a notice of statutory intervention, pursuant to G.L. c. 12, § 11E. Evidentiary hearings were held on March 14, 15 and 22, 2000. The Company sponsored the testimony of two witnesses: Dr. Susan F. Tierney, director of Lexecon, Inc.; and Karen Asbury, director of Regulatory Services for Unitil Service Corp. The Attorney General sponsored the testimony of Timothy Newhard, a financial analyst with its Regulated Industries Division.

On April 19, 2000, after the close of the record in this case, the Department was able to retrieve the CGAC filings made by the Company during the years 1987-1992 that the Company and Department had previously been unable to locate. As a result, the Department re-opened the evidentiary record. Additional evidentiary hearings were held on February 14 and 15, 2001. The Company sponsored the testimony of four witnesses: Scott A. Ferrari and David W. Graham, former Fitchburg employees responsible for the CGAC filings during the relevant periods under investigation; James Harrison, vice-president of Management Applications Consulting, Inc., and a consultant to Fitchburg in preparing its cost-of-service study ("COSS") in D.T.E. 98-51; and supplemental testimony from Ms. Asbury. The Attorney General sponsored the supplemental testimony of Mr. Newhard. Fitchburg and the Attorney General filed briefs and reply briefs.

III. OUTSTANDING MATTERS

There are two outstanding matters the Department must address: (1) Fitchburg's March 28, 2000 appeal of a Hearing Officer's ruling regarding the admissibility of testimony about discussions leading to the 1984 Settlement, and (2) Fitchburg's February

16, 2001 appeal of a Hearing Officer's ruling regarding the admissibility of notes and analysis of a former Department employee.

A. Fitchburg's Appeal Regarding Disclosure of Settlement Discussions

During evidentiary hearings, the Department staff questioned the Attorney General's witness about the 1984 Settlement (Tr. 3, at 408-411).[(4)] Fitchburg objected to this line of questions, arguing that the parties agreed in the 1984 Settlement that all settlement discussions would be confidential and, further, that the Department approved the settlement, including the confidentiality provision (id., at 409). The Hearing Officer denied Fitchburg's objection to the admissibility of questions relating to the substance of the settlement negotiations and ruled that the Department's questions would be answered on a sealed record (id., at 410). The Attorney General did not object to the Hearing Officer's ruling (id.).

On March 28, 2000, Fitchburg filed an appeal of the Hearing Officer's ruling ("Fitchburg Appeal"). The Company sought to exclude these settlement discussions, not based on privilege, but rather based on the 1984 Settlement (including its confidentiality provisions) that was approved by the Department (Fitchburg Appeal at 4-5). Fitchburg argued that the Department's inquiries into the substance of the parties' negotiations in D.P.U. 84-145 are contrary to the Department's prior approval of the 1984 Settlement containing a provision that settlement discussions would not be used in future proceedings (Fitchburg Appeal at 3). The Attorney General did not comment on the Fitchburg Appeal.

The issue of the proper treatment of settlement discussions and the evidentiary exclusion of settlement offers is not novel to the Department. The Department's long-standing policy on this subject is explicitly set forth in Boston Gas Company, D.P.U. 88-67 (1988). In that Order, the Department determined that parties to a proceeding before the Department who engage in compromise discussions, do not possess a right to exclude from evidence information necessary for the Department to conduct an investigation of matters within its purview. Id. at 25. However, the Department recognized that in "limited" circumstances, parties wishing to have these discussions shielded from Department inquiry, must make a motion in limine to exclude from evidence any reference to all or part of the negotiations. Id. at 24.[(5)]

While the 1984 Settlement was approved by the Department before the decision in D.P.U. 88-67 was issued, prior Department precedent was to consider independent facts arising out of settlement discussions or offers of settlement as discoverable information.[(6)] In Edgartown Water Company, D.P.U. 62 (1980), the Department stated that stipulations by parties are scrutinized with the same intensity as any other filing. D.P.U. 62, at 13 (1980) (stipulation as to the cost of equity, capital structure and interest expense is scrutinized like any other filing). Here, simply because the Department approved the parties' Motion for Settlement, there is no law, rule or regulation that prohibits the Department from later scrutinizing information found in D.P.U. 84-145. The details of what costs were or were not included in the settlement agreement are independent facts

and not the type of admissions as to the validity of another party's claim that the Department recognizes may be shielded from inquiry. For these reasons, the Hearing Officer's ruling regarding the admissibility of questions about the 1984 Settlement is affirmed.

B. Fitchburg's Motion Regarding the Exclusion of Notes and Analysis

Fitchburg sought to introduce as evidence the notes and analysis of a Department employee regarding the Department's investigation of the Company's CGAC filings made between 1987 and 1992. These notes were appended to the supplemental prefiled testimony of Ms. Asbury. At the February 14, 2001 evidentiary hearing, the Hearing Officer excluded these notes from evidence because the former Department employee did not have any decision making authority when reviewing the Company's CGAC filings, and consequently, this person's notes and analyses had no probative value to the Department's investigation (Tr. 4, at 483-484).

On February 16, 2001, the Company filed an appeal of the Hearing Officer's ruling (Fitchburg Second Appeal). Fitchburg requests that the former employee's notes and analysis be entered into the record in this proceeding (Fitchburg Second Appeal at 10). Alternatively, Fitchburg requests the opportunity to reopen the evidentiary record and to examine the former Department employee as a witness (id.). Fitchburg contends that the notes and analysis are materially relevant and provide "valuable circumstantial evidence that [Fitchburg] was not hiding, subverting or obscuring IFC recovery from the Department and are consistent with, and act to corroborate, the testimony of other sworn witnesses in the proceeding" (id. at 2).

On February 23, 2001, the Attorney General filed a reply to Fitchburg's Second Appeal ("Attorney General Reply"). The Attorney General maintains that the notes of the former Department employee are not relevant to the issues presented before the Department because the notes do not prove or disprove a material fact in the case and, therefore, requests that the Hearing Officer's ruling be affirmed (Attorney General's Reply at 3).

The 1987-1992 CGAC filings for gas distribution companies, including Fitchburg, were located in several boxes in the Department's new offices (Tr. 4, at 507). The boxes included the CGAC filings, Department approval letters, internal notes and analyses of a former Department staff member. When the CGAC filings were provided to the parties, the notes and analyses were inadvertently also made available. At the hearing, the Company stated that when there were questions concerning one of its CGAC filings, the matter was typically resolved over the telephone or during a visit by the Company's employees to the Department's offices (Tr. 4, at 464-465). Therefore, the internal staff notes and analyses have no value in proving or disproving whether Fitchburg had any information that a problem existed with the manner in which it had filed its CGAC. Additionally, because the former Department employee had no decision-making authority, his internal review and recommendations are not relevant to prove a particular fact material to an issue in this proceeding. Therefore, we affirm the Hearing Officer ruling.

We also reject Fitchburg's requested alternative relief to re-open the record and call the former Department employee as a witness. Because the notes were properly excluded, the former Department employee's testimony on the same subject is also excluded on the same grounds. In addition, the Company has had ample opportunity to present witnesses, and has provided no reason to justify calling this additional witness after the record has been closed. IV. POSITIONS OF THE PARTIES

A. Attorney General

1. Burden of Proof

The Attorney General contends the current proceeding is an investigation of an issue reserved by the Department's earlier approvals of Fitchburg's CGAC filings. Therefore, the Attorney General argues that the Company bears the burden of proof on the question of whether IFCs are appropriately included within its CGAC charge (Attorney General Reply Brief at 6).

2. Overcollection

The Attorney General states that between 1987 and 1998, Fitchburg overcollected $675,052 by concurrently collecting IFCs through its base rates and its CGAC reconciliation (Attorney General Brief at 11, 14). As support, the Attorney General argues that in D.T.E. 98-51, the Department determined that IFCs included in the Company's CGAC from 1987 to 1998 did not comply with the requirements set forth in Cost of Gas Adjustment Clause Rulemaking, D.T.E. 1669-A (1986), 1669-B (1987), 1669-C (1987) as codified in 220 C.M.R. § 6.06 (Attorney General Brief at 14, citing DTE 98-51, at 21). The Attorney General further argues that the requirements of 220 C.M.R. § 6.06 mandate the use of a financing vehicle or trust to finance inventory charges as a pre-condition for collecting these charges in the CGAC (id.). Therefore, the Attorney General concludes that the $675,052 had not been collected through an approved financing vehicle, and thus that the overcollection should be refunded to Fitchburg's customers (id.).

In addition, the Attorney General argues that it is logical to conclude that, prior to D.P.U. 1669-C, IFCs were included in the computation of the Company's rate base used to determine its base rates (id. at 8). In support, the Attorney General notes that in reviewing the 1984 Settlement, the Department assessed the revenue requirements proposed by the settlement in light of the test year cost of service, other information filed in the case, and the Department's own precedent which included gas IFCs in base rates (Attorney General Reply Brief at 8, citing Tr. 2, at 252-254). Therefore, the Attorney General argues that "the only conclusion can be" that IFCs were included in the base rates resulting from D.P.U. 84-145 (Attorney General Reply Brief at 8). The Attorney General states that because IFCs were included in the base rates established in both D.P.U. 1214 and D.P.U. 84-145, "any dollar amount recovered simultaneously through the CGAC would be *per se* an overcollection that must be returned to customers" (id. at 9).

The Attorney General contends that Fitchburg's base rates are not at issue here, but rather its CGAC (id. at 10). Even assuming that the Company's claimed rate of return during this period is relevant, the Attorney General states that the basis for Fitchburg's calculations have not been weather-normalized and do not conform to the methods used by the Department (id. citing Tr. 2, at 257).

3. Refund

The Attorney General asserts that requiring a refund of the Company's overcollection is the correct regulatory approach and would not constitute improper retroactive ratemaking (Attorney General Brief at 16). As evidence that the CGAC is not a "fixed" or "final" rate, the Attorney General cites the language of the Department's generic CGAC approval letter (id. at 17, citing Exh. FGE-3, Att. B). The Attorney General argues that, given the retrospective and reconciling nature of fuel adjustment clauses in general, the Company cannot claim it was not on notice that the Department could later impose adjustments and require refunds in connection with the CGAC (id. at 18). In addition, the Attorney General states that Fitchburg never appealed, sought reconsideration of or otherwise challenged the Department's characterization of the CGAC approvals (Attorney General Reply Brief at 11). As such, the Attorney General argues that the Company accepted the Department's CGAC terms (id.).

The Attorney General further argues that whether the Company's base rates were the result of a settlement or of a fully litigated rate case is irrelevant to whether the Company should be required to refund any overcollections to its ratepayers (Attorney General Brief at 19). According to the Attorney General, the record suggests that Fitchburg's base rates, both as a result of the stipulated revenue requirement in D.P.U. 84-145 and its last adjudicated rate case in D.P.U. 1214, contained gas inventory finance charges (id. at 19-20). The Attorney General asserts that had Fitchburg sought to collect the IFCs through the proper vehicle as is required in 220 C.M.R. § 6.06, the Department would have followed its past practice and deferred approval of the inclusion of finance costs in the CGAC until it was clear that these costs were not also included in the Company's base rates (id. at 19, citing Boston Gas Company, D.P.U. 88-67, at 30 (1988)).

As a result of the overcollection, the Attorney General argues that the Company must refund its ratepayers $675,052 with interest computed from 1987 through 1998 (Attorney General Brief at 21). The Attorney General suggests that the use of a 15 per cent interest rate is reasonable because it represents the opportunity cost of the Company's ratepayers and their available consumer credit through various retail stores (Exh. AG-1, at 14-15.).

B. Fitchburg Gas and Electric Light Company

1. Burden of Proof

Fitchburg asserts this investigation was instituted by the Department pursuant to allegations set forth by the Attorney General. As such, Fitchburg argues that the Department and the Attorney General have the burden of proof and must demonstrate through "substantial evidence" the existence of an overcollection (Fitchburg Brief at 6, 9, citing Medical Malpractice Joint Underwriting Ass'n of Mass. v. Commissioner of Ins., ("MMJUA") 395 Mass. 43, 47-48 (1985)).

2. Overcollection

Fitchburg argues that, in order to find that it overcollected gas IFCs, the Attorney General must show that: (1) there is an "identifiable" amount of gas inventory in the Company's rate base; and (2) the Company was "unreasonable in its interpretation" of D.P.U. 1669, 220 C.M.R. § 6.06, and each of the CGAC filings made by the Company since 1987 (id. at 9-10). The Company argues that the Attorney General has not met his burden of proof on the present record (id.).

With respect to its base rates, Fitchburg argues that because D.P.U. 84-145 was a settled rate case, it is impossible to know the dollar amount, if any, of IFCs that may have been included in rate base (id. at 10). Fitchburg argues that the rates approved by the Department in D.P.U. 84-145 were based on a settlement for an overall revenue requirement and "are not directly or specifically connected to the elements of the proposed 1983 test year cost of service" (id. at 12-13). Fitchburg argues that any attempt to upset or look behind the settled revenue requirements in D.P.U. 84-145 is an effort to retroactively reform rates

(id. at 37).

With respect to the CGAC regulations promulgated by the Department in 1987, Fitchburg contends that D.P.U. 1669-C did not explicitly require: (1) Department pre-approval of an inventory financing mechanism, (2) a trust, or (3) a base rate proceeding (Fitchburg Reply Brief at 7). Fitchburg argues that, pursuant to D.P.U. 1669-C, it was permitted to recover IFCs through the internal financing vehicle established in Fitchburg Gas and Electric Light Company/UMC Electric Company, Inc., D.P.U. 89-66 (1992) (Fitchburg Brief at 22-23, Reply Brief at 7). As support for its argument that a base rate proceeding was not required, the Company argues that the draft regulations contained in D.P.U. 1669-A did require conducting a base rate proceeding for each company prior to the implementation of the 1987 CGAC, but that the Department did not include such a requirement in the final regulations contained in D.P.U. 1669-C (Fitchburg Reply Brief at 7).

The Company argues that, because it cannot be shown that Fitchburg failed to follow a Department directive or precedential direction, an overcollection cannot be proven (id. at 8). Fitchburg further argues that, even if it were found to have failed to follow a Department directive or precedent, it must also be shown that it was "unreasonable" in its failure to follow the Department's directives (id.). The Company contends that it was reasonable in its reliance on the Department's continuous approval of its CGAC filings

from 1987-1998 (Fitchburg Brief at 25-27). Fitchburg argues that, based on what it knew or should have known, it reasonably interpreted the CGAC regulations to permit the inclusion of interest on gas inventory

(id. at 23). Finally, the Company argues that the Department's prior inventory finance orders pursuant to G.L. c. 164, § 17A did not constitute general notice to the industry that IFCs must be removed from base rates, especially in light of the later promulgation of 220 C.M.R. § 6.06 (id. at 28).

The Company also argues that public policy militates against ordering reimbursement upon a finding an overcollection. The Company argues that there is a recognized public policy in limiting the time within which liability can attach under law, because of the difficulties inherent in defending against a claim "where evidence has been lost, memories have faded, and witnesses have disappeared" (Fitchburg Brief at 33-34, citing Klein v. Catlano, 386 Mass, 701, 709 (1982)). In addition, Fitchburg argues that an overcollection can only be established if the Department rejects the legal premise that the Company is entitled to rely upon the Department's final orders (id. at 34-37). Finally, Fitchburg argues that its rates were continuously within the "zone of reasonableness" throughout the time period in question, and that the Company's gas operations have earned less than the rate of return allowed in both D.P.U. 84-145 and D.P.U. 98-51 (Fitchburg Brief at 44, Fitchburg Reply Brief at 13). As such, Fitchburg argues that the Department has the authority to allow these rates as just and reasonable (Fitchburg Brief at 44, Fitchburg Reply Brief at 13). The Company suggests that its reliance on the Department's approvals of its CGAC filings had influenced Fitchburg's decision not to file a base rate proceeding for its gas operations (Fitchburg Brief at 45).

3. Refund

The Company argues that the Department does not have the authority to impose reparation, refunds, or penalties, or to retroactively set Fitchburg's rates (Fitchburg Brief at 37-44). Fitchburg argues that this lack of authority to order reimbursement of collected charges to customers is "equally applicable to base rate collections and as it is to rates established under purchased gas adjustment clauses" (id. at 39, citing Lowell Gas Company v. Attorney General, 377 Mass. 37, 45, 385 N.E.2d 240, 246 (1979) and Boston Edison Company v. Department of Public Utilities, 375 Mass. 1, 6; 375 N.E.2d 305, 312 (1978)). Fitchburg argues that the only retroactive rate authority granted the Department over gas companies is to allow adjustments in its cost of gas to reflect FERC-approved refunds (id. at 42, citing G.L. c. 164, § 94F). The Company contends that, unlike the case in Automobile Insurance Bureau of Massachusetts v. Commissioner of Insurance, 425 Mass. 262 (1997) ("AIBM"), the Department "can not look to a specific statute for upward and downward adjustments in a CGA" (id. at 41, citing AIBM at 265).

In addition, the Company contends that substantial evidence does not support the Attorney General's 15 percent interest rate and categorizes this rate as a "penalty" (Fitchburg Brief at 33). The Company argues that there is no evidence that a 15 percent interest rate represents the opportunity cost of Fitchburg's ratepayers and their available

consumer credit (id.). Fitchburg maintains that imposing such a penalty would be unreasonable because there is no substantial evidence that an overcollection exists (id.). Even if an overcollection did exist, the Company argues that requiring a refund with such a high interest rate would be "arbitrary and capricious" (id.)

V. ANALYSIS AND FINDINGS

A. Burden of Proof

The first issue the Department must address is which party bears the burden of proof in this case. Both the Attorney General and the Company claim that each other has the burden of proof. The Attorney General argues that, because this proceeding is an investigation of an issue reserved by the Department's earlier tentative approvals of Fitchburg's CGAC filings, the Company has the burden of proof (Attorney General Reply Brief at 6). Fitchburg argues that since the Department initiated this investigation based on allegations raised by the Attorney General, the burden of proof rests with both the Department and the Attorney General (Fitchburg Brief at 9, citing MMJUA at 47-48).

The case at issue here is distinguishable from the MMJUA case. In the MMJUA case, the Court noted that the statute authorized the Insurance Commissioner not only to approve or to disallow proposed medical malpractice rates, but actually to set medical malpractice rates. Id. at 47. The Court contrasted this authority with the statutory functions of other state agencies, including the regulation of public utility rates set forth in G.L. c. 164, § 94. The Court concluded that this difference in statutory duties warranted a different standard of proof. Id. at 47-51.

In contrast, the Supreme Judicial Court has stated that with respect to a company's obligations in a Department investigation:

Within a substantial range, business decisions are matters for the Company's determination. See New England Tel. & Tel. Co. v. Department of Pub. Utils., 371 Mass. 67, 84 (1976), and cases cited; Weld v. Gas & Elec. Light Comm'rs., 197 Mass. 556, 560 (1908). Even in such matters, however, the Company when challenged must come forward with evidence to explain its decisions and show that they are not inconsistent with valid policies enforced by the Department. New England Tel. & Tel. Co. v. Department of Pub. Utils., 360 Mass. 443, 493 (1971).

Fitchburg Gas and Electric Light Co. v. Department of Public Utilities, 375 Mass. 571, 578-579 (1978).

Thus, once the issue of a potential overcollection was properly raised by the Department, the burden rests with Fitchburg "to come forward with evidence to explain its decisions and show that they are not inconsistent with valid policies enforced by the Department." Id. As noted above, this case resulted from an investigation into a proposed increase in base rates filed by Fitchburg pursuant to G.L. c. 164, § 94, during which time information was developed concerning the Company's treatment of IFCs. Insofar as this case arose

from a § 94 investigation in which the petitioning utility bears the burden of proof, the Department finds that Fitchburg also bears the burden of proof in this proceeding. Fryer v. Department of Public Utilities, 374 Mass. 685 (1978); Metropolitan Dist. Commission v. Department of Public Utilities, 352 Mass. 18 (1967). See also Boston Edison Company, D.P.U. 97-95, at 5-7, Interlocutory Order on: (1) Motion for Order of Burden of Proof, (2) Proposed Nondisclosure Agreement, and (3) Requests for Protective Treatment (July 2, 1998). Moreover, insofar as this case arose from the operation of the CGAC, it implicates a reconciling mechanism that lies outside the retroactive ratemaking stricture that constrains Department action under G.L. c. 164, § 94.

B. Overcollection

Having established that the burden of proof lies with Fitchburg, we must next look at whether an overcollection of gas IFCs has occurred. Fitchburg argues that an overcollection can not be established absent proof of an "identifiable" or "discernable" amount of gas IFCs in base rates. It further argues that, because the base rates in effect during the period in question were the result of a settlement that did not provide for a stipulated amount for any individual base rate items, it is impossible to determine the amount of gas IFCs in base rates. We do not agree. It is not necessary for the Department to determine the exact dollar amount of IFCs contained in base rates in order to find whether the Company has overcollected. Instead, we must first determine whether the Company's base rates, as established in D.P.U. 1214 and D.P.U. 84-145 allowed Fitchburg the opportunity to recover gas IFCs, whatever the amount these costs may have been. If this is the case, any amount of gas IFCs simultaneously recovered through the CGAC could be considered an overcollection.

Prior to the promulgation of the CGAC regulations, the practice of including IFCs as a component of materials and supplies in rate base was consistent with Department precedent. In 1983, the Company requested, and the Department approved, the inclusion of gas inventory as a component of the working capital requirement used to determine base rates. D.P.U. 1214, at 87; Exhs. FGE-2, at 13-14; AG-1, at 5; DTE 3-9. See also D.P.U. 1100, at 6-11; D.P.U. 19666/19677, at 14-15. Under the rate structure approved in D.P.U. 1214, Fitchburg recovered interest on gas inventory through a materials and supplies component in rate base. Fitchburg requested a gas rate increase again in D.P.U. 84-145 (1984). In that case, the Company again proposed to collect interest on inventory through a return on rate base (Exhs. AG-1 at 5; FGE-2, at 9). Ultimately, the Company submitted a settlement negotiated with the Attorney General. The Department approved the settlement based on a stipulated revenue requirement, without any specification as to what cost items or cost levels were included in the settlement. D.P.U. 84-145, at 3-5. There is no discussion of gas IFCs in the settlement.

The fact that base rates were established as a result of a settlement without specification as to the amount of any cost items or cost levels, does not mean that those specific costs are not being recovered. Unless a settlement expressly excludes, adjusts, or otherwise disturbs a requested cost element recovery, established ratemaking principles consider a settlement to incorporate all of the company's cost categories necessary to provide

service. Consistent with Department precedent, Fitchburg was recovering IFCs through base rates prior to the 1984 Settlement. The Company included gas IFCs in its cost of service in both D.P.U. 1214 and D.P.U. 84-145. The 1984 Settlement did not exclude the collection of IFCs in Fitchburg's base rates. The core features of the 1984 Settlement, in relevant part, merely reduced the requested gas rate increase for gas operations by $634,675. In view of the then long-standing Department precedent on the inclusion of gas inventories as a component of rate base and its consistent application by Fitchburg, it is reasonable to conclude that a certain amount for Fitchburg's gas inventory costs was included in the stipulated base rates. Fitchburg's admission that a zero level of gas inventory would have been inconsistent with the Company's obligation to meet winter or peak customer demands further militates for the inclusion of gas inventory costs in Fitchburg's overall cost of service (Tr. 2, at 197-201).[(7)] Therefore, based on the foregoing analysis, the Department finds that Fitchburg's base rates in effect between 1985 and 1998 allowed Fitchburg the opportunity to recover gas IFCs.

Fitchburg would have us believe that, although it collected IFCs in rates after D.P.U. 1214, although it sought recovery of IFCs in its D.P.U. 84-145 COSS, and although its D.T.E. 98-51 COSS once again sought IFC recovery - that, in short, despite all this, IFCs were somehow omitted from rates for the 14 years between the 1984 Settlement and the D.T.E. 98-51 rate filing. The claim is just untenable.

As recognized by Fitchburg, a COSS states representative costs of service based on an *actual*, historic test year. Apart from post-test year adjustments, the elements of a COSS are *actual* costs incurred in the test year (D.T.E. 98-51, Exh. FGE JLH-1, at 14-15).

Mr. Harrison sponsored the COSS in D.T.E. 98-51 (id. at 1-2). During the proceeding,

Mr. Harrison adopted the COSS with limited corrections (D.T.E. 98-51, Tr. 6, at 6-10). These limited corrections did not encompass the Company's treatment of the test-year IFCs (id.). Rather, it was only when asked later in the proceeding, that Fitchburg explained it was not their "intent to double count [the IFCs]" but that when the COSS was prepared, the Company was unsure whether such costs would ultimately be collected in base rates or through the CGAC (D.T.E. 98-51, Tr. 12, at 87-88). Fitchburg's later characterization of inclusion of IFCs in its D.T.E. 98-51 COSS as a "placeholder" is, to put it with restraint, implausible. In fact, the inclusion is, when looked at logically, far more in the nature of an admission by the Company in its filing, albeit now inconvenient to or against the interest of its present claim, to the effect that the Company considered IFCs to be part of its established rates dating from D.P.U. 84-145.

The Company cites the holding in Boston Consolidated Gas Company v. Department of Public Utilities, 321 Mass. 259 (1947) ("Boston Consolidated") for the proposition that it is entitled to rely on the plain wording of D.P.U. 84-145 and that the Department cannot "look behind" this decision to impute individual cost components to the settlement (Fitchburg Initial Brief at 34-37). However unlike the case in Boston Consolidated, there is nothing in the plain language of D.P.U. 84-145 to preclude a finding that Fitchburg's base rates include IFCs. D.P.U. 84-145 states: "the parties shall not be deemed to have

admitted any allegation presented in the proceeding nor would the acceptance of the proposal constitute a determination by the Department on the merits of any allegation or contention made by the parties during the course of the proceeding." D.P.U. 84-145, at 3. This language merely recognizes that the Department reviews the terms of the settlement, does an independent analysis of the likely outcome under a litigated proceeding and makes its own determination whether the terms of the settlement are consistent with the outcome in the absence of a settlement, without the need to accept or reject any positions that may have been taken by parties during settlement negotiations. Taking Fitchburg's argument to its full logical extension, the Company would have us believe that, after a settlement, there simply are no longer any identifiable cost components included in its base rates. This is clearly not the case -- the 1984 Settlement did not specifically preclude the collection of IFCs in base rates or, for that matter, any specific cost item that was proposed in the Company's initial rate filing. In the absence of evidence to the contrary, such as other settlement terms or appended schedules, we consider the 1984 Settlement to have simply reduced the overall revenue requirement, but did not eliminate any particular cost-of-service element or account originally filed-for. The silence of a settlement on some point does not necessarily negative an established practice or, for that matter, strip that practice of the endorsement of precedent, especially where, as here, the practice was memorialized in the petitioner's case-in-chief and in rates in force at the time of filing.

Having found that Fitchburg was collecting IFCs in base rates, we now must determine whether Fitchburg also collected IFCs through its CGAC. As discussed above, the Department amended its CGAC regulations in 1986 and 1987 to allow gas utilities to adjust their rates for firm gas sales on a semi-annual basis. D.T.E. 1669-A; D.T.E. 1669-B; D.T.E. 1669-C. Fitchburg's books demonstrate that it collected $675,052 in IFC charges through the CGAC from 1987 through 1998. This amount, which we find to be an overcollection of IFC charges, is undisputed by the parties.

The regulations require a company to use a financing vehicle or trust to finance inventory charges for collecting these charges in the CGAC, or to petition the Department for an exemption from the regulations. See 220 C.M.R. §§ 6.06, 6.12. Long-standing Department precedent conditions approval of gas inventory financing vehicles on terms that preclude any simultaneous recognition of IFCs in both base rates and the CGAC. Colonial Gas Company, D.P.U. 1126, at 6-7 (1982); Bay State Gas Company, D.P.U. 962, at 12 (1982); Haverhill Gas Company, D.P.U. 246, at 11 (1980); Boston Gas Company, D.P.U. 123, at 11-12 (1980).[(8)] To do otherwise would force a company's ratepayers to pay for these costs twice. The promulgation of the amended CGAC regulations in D.P.U. 1669-C did not alter this precedent. While the Company claims that the Department's prior inventory financing orders did not constitute general notice to the industry about the appropriate treatment of IFCs, the Department has frequently used its regulatory proceedings as a vehicle to inform companies about our policies. See Colonial Gas Company, D.P.U. 84-96, at 8-9 (1984); Boston Edison Company, Policy Statement of the Commission Concerning the Adoption of Year-End Rate Base, D.P.U. 160 (1980).[(9)] It is Fitchburg's duty to stay abreast of regulatory developments that affect its obligations to its customers and its business practices. This principle is so ancient as to be axiomatic: *ignorantia legis neminem excusat*.

Although Fitchburg argues that it had an approved financing vehicle as set forth in D.P.U. 89-66, the Department's approval in D.P.U. 89-66 pertained to the approval of a cash pooling and loan agreement whereby Fitchburg, as a newly-acquired subsidiary of UNITIL, could deposit surplus cash into a pool from which participants could borrow to meet daily working cash requirements. D.P.U. 89-66, at 3. While a cash pooling agreement offers utilities potential efficiencies in overall cash management, cash pooling agreements serve a different purpose from the inventory trust agreements specified in 220 C.M.R. § 6.06. An inventory trust serves as a means to meet a specific component of a utility's overall operating requirements through an interest component applied to the monthly average of inventory being financed. 220 C.M.R. § 6.06. Therefore, the Company's cash pooling agreement in D.P.U. 89-66 is by no means an "other financing vehicle" as specified in 220 C.M.R. § 6.06.[(10)]

With respect to the Company's position that it had operated reasonably in reliance on the Department's previous approvals of its CGAC filings, it is clear that the Department should not have approved these CGAC filings including IFCs while the Company was concurrently collecting IFCs in its CGAC and base rates. This occurred, in part, because Fitchburg had not sought approval of its financing vehicle before modifying the application of its CGAC. Even assuming the Company reasonably relied upon the Department's previous approvals of Fitchburg's CGAC filings and possible discussions with Department staff about the application of 220 C.M.R. § 6.00, Fitchburg should not have begun collecting IFCs through the CGAC without first seeking an adjustment in its base rates. Cf. Boston Gas Company, D.P.U. 88-67, at 28-32 (company removed gas inventory from rate base as part of proposal to collect all financing costs through CGAC). Fitchburg also began collecting IFCs through the CGAC without first seeking approval of an appropriate financing vehicle, pursuant to 220 C.M.R. § 6.06. For these reasons, we find that Fitchburg's actions concerning its IFCs resulted in an unlawful levy on its customers. Fitchburg knew or, as a reasonable, prudent provider of gas service, should have known that it had no right to charge customers for IFCs in the CGAC until it had eliminated, as all the other gas companies did, IFC recovery in base rates. The fact that overrecovery went unrecognized by earlier Commissions does not mean that the present Commission is powerless to correct an injustice to ratepayers -- especially where it is perpetrated through, and correctable by, a reconciling mechanism.

As a matter of public policy, the Company cannot reap the benefits of the overcollection. The Department's obligation to protect the public interest requires that ratepayers be made whole for this CGAC overcollection. While the Company argues that its gas rates have earned less than their allowed return and, further, that Fitchburg has foregone the opportunity to seek a base rate increase over this period, the reasonableness of Fitchburg's base rates is not at issue here. Allowing the Company to retain the overcollection, merely on the basis of Fitchburg's failure to earn up to its allowed return, would effectively grant Fitchburg a base rate increase without the proper ratemaking proceeding. Doing so, moreover, would be inconsistent with G.L. c. 164, § 94. In addition, what we face here is a CGAC overcollection issue, and it must be addressed in accordance with the provisions of the CGAC.

C. Refund

Fitchburg argues that, even assuming an overcollection of IFCs occurred in the Company's CGAC, the Department is precluded from adjusting Fitchburg's rates because of: (1) the prohibition against retroactive ratemaking; and (2) public policy considerations limiting the amount of time during which an adjustment may be properly made. In contrast, the Attorney General contends that the reconciliation mechanism contained in 220 C.M.R. § 6.00 is explicitly intended to provide for adjustments to a utility's CGAC, and that public policy requires an assurance against incorrect regulatory practices, regardless of when those practices may have taken place.

Concerning the issue of retroactive ratemaking, we note as an initial matter that the Company's base rates established in D.P.U. 84-145 are not affected by this proceeding. The focus of this investigation is whether Fitchburg improperly collected IFCs in the CGAC.[(11)] Accordingly, any adjustments or refunds directed by the Department through this Order would have to be implemented through the CGAC. The CGAC, as most recently embodied by 220 C.M.R. § 6.00, has long featured a reconciliation mechanism intended to ensure that a gas utility fully recovers its costs of gas, and that only approved gas-related costs are recovered through the CGAC. 220 C.M.R. §§ 6.06, 6.08; D.P.U. 1669-C at 10-11; Blackstone Gas Company, D.P.U. 511, at 10 (1981); Blackstone Gas Company, D.P.U. 192, at 30-31 (1980); Standard Cost of Gas Adjustment Clause, D.P.U. 19806-A/20170, Att. 1, at 4 (1980); Standard Cost of Gas Adjustment Clause, D.P.U. 4240-78/19806, Att. 1, at 5 (1979).

The reconciliation features of the CGAC are kindred to the reconciliation mechanism found in the Insurance Commission's safe driver insurance plan, which has been upheld by the Supreme Judicial Court. AIBM at 265. See also D.T.E. 98-51, at 21 n.8 (1998). Fitchburg argues that AIBM does not in any way change or enlarge the statutory restrictions of the Department's own authority to require refunds and that the only retroactive rate authority granted to the Department is to allow adjustments in a company's cost of gas to account for FERC-approved refunds (Fitchburg Initial Brief at 42). We disagree. The Massachusetts decisions relied upon by the Company, e.g., Lowell Gas Co., 377 Mass. 37 (1979) and Boston Edison Co., 375 Mass. 1 (1978) were decided before the 1987 CGAC regulations. The 1987 CGAC regulations established a method for appropriately collecting IFCs and expressly grant only "tentative" approval of the requested Gas Adjustment Factor and specifically reserves the right "to require the Company" to issue customer "refunds." See, e.g., Exh. FGE-3, Att. B.

Companies have long been on notice that the CGAC is not intended to produce a final rate, but rather is intended as a fully-reconciling mechanism. The approval of a CGAC factor is subject to the refund of any amounts found by the Department to be the result of "imprudent" company action, upon subsequent review (id.). As part of the Department's approvals of Fitchburg's CGAC filings, as with the CGAC filings of other gas utilities, we have long included the following language:

The Department will therefore allow the application of the GAF, but reserves the right to change the factor or the method of computation or to require the Company to refund to its customers [emphasis added] any amounts that are found by the Department to be the result of imprudent Company action in the event that subsequent review of the Company's filings or any other relevant information filed with the Department requires such changes, or if a new standard clause is promulgated by the Department.

Exh. FGE-3 (2/14/2001), Att. B.

As acknowledged above, approval of the Company's CGAC filings containing IFCs between 1987 and 1998 was in error. Based on clear Department precedent, we would not have approved CGAC filings including IFCs while these same costs were being recovered in the Company's base rates. Fitchburg's own witness acknowledged a distinction between correcting for errors and ex post facto interpretations of regulations in stating:

If there were a clear mistake, as opposed to a difference of opinion about interpretation of policy or interpretation of the application of rules, and it was clear finding of a mistake, then the Department, I suppose subject to its organic authorities, can take a look back.

Tr. 1, at 137-138.

The CGAC mechanism is both appropriate and well-suited as a vehicle for making prospective corrections for past errors. Any regulatory burden associated with this proceeding is outweighed by the public policy benefits of ratepayers enjoying the benefit of sound regulatory practices in place to ensure that rates are just and reasonable. Cf. Manufactured Gas Process, D.P.U. 89-161, at 46-48 (1990) (the passage of time, unavailability of witnesses, and state of company records rendered it unlikely that individual prudence reviews of manufactured gas plants and processes over the period 1822 through 1978 would result in equitable outcomes). As noted above, both parties agree that the Company collected $675,052 in gas inventory charges through the CGAC between May of 1987 and November of 1998 (Exhs. FGE-2, at 8; AG-1, at 3). Based on the above, because the Company was concurrently collecting these same costs through its base rates, the Department finds that the Company overcollected $675,052 in gas inventory costs during this period through the CGAC which must be returned to ratepayers. This Department's long-ago oversight and the Company's almost 12-year silence are no reasons to leave ratepayers without a remedy. Ratesetting is not

MONOPOLY®. The Department's Order in D.P.U. 84-145 was not a "Community Chest" card reading "Bank error in your favor. Collect $675,052 from the CGAC." Equitable treatment of ratepayers requires that this unjust enrichment be disgorged and the CGAC mechanism permits, indeed requires, that it be.

Having determined that Fitchburg overcollected $675,052 through its CGAC between 1987 and 1998, and that it is appropriate to return this overcollection to ratepayers, it is necessary to determine the appropriate carrying charges that must be added to the balance in order to fully compensate the Company's ratepayers. While the Attorney General suggests an interest rate of 15 percent equal to customer opportunity costs, the supporting evidence presented here, consisting of interest rates charged by several retail companies on credit card purchases, and opinion testimony (Exh. FGE 1-23; Tr. 3, at 398-401), lacks sufficient foundation to rely upon as a measure of appropriate carrying charges.

The Company has been paying and earning the prime interest rate on its CGAC over and undercollections (Exh. AG 1-7). See also 220 C.M.R. § 6.08. This interest rate is integral to the operation of the CGAC and represents a fair and reasonable interest rate to be applied to the overcollection. Accordingly, the Company is directed to apply interest on the overcollection. Such interest shall be the average monthly weighted prime interest rate and be applied to the average monthly outstanding balances. See Blackstone Gas Company, D.P.U. 511, at 9 (1981). The Company shall apply this interest rate to the unamortized balance.

In determining the appropriate amortization period, the Department must balance the interests of the Company and its ratepayers, taking into consideration such factors as the amount under consideration for amortization, the value of such an amount to ratepayers based on certain amortization periods, and the effect of the adjustment on the utility's finances and income. See Barnstable Water Company, D.P.U. 93-223-B at 14 (1994); Fitchburg Gas and Electric Light Company, D.P.U. 84-145-A at 54 (1985); Boston Edison Company, D.P.U. 906, at 244 (1982). The Company reported that its net income associated with gas operations has ranged between a negative 0.76 percent and 11.54 percent, with recent returns of five percent or less (Exh. FGE-2, Sch. KMA-6). In view of this financial performance, the Department finds that a one-year passback of the overcollection could result in serious financial harm to the Company, harm that might rebound on service to ratepayers.[(12)] There is no reason to risk and every reason to avoid incurring such harm. A fair solution can be fashioned without running the risk.

As noted above, Fitchburg began collecting inventory finance charges through its CGAC on May 1, 1987 (Exh. FGE-2, at 7). The Company's base rates continued to include inventory finance charges until November 30, 1998, resulting in a period of 11 years and seven months of overcollections. An amortization period commensurate with the period during which CGAC overcollections took place strikes an appropriate balance between the need to make ratepayers whole for the overcharges and the need to maintain the financial integrity of the Company. Accordingly, the Department finds that an amortization period not to exceed 139 months is appropriate.

VI. ORDER

Accordingly, after notice, hearing, and consideration, it is hereby

ORDERED: That Fitchburg Gas and Electric Light Company shall file within thirty (30) days from the date of this Order a revised CGAC reconciliation factor to include an additional $675,052 plus interest accrued as of May 1, 1987; and it is

FURTHER ORDERED: That Fitchburg Gas and Electric Light Company shall calculate the accumulated interest on the aforementioned $675,052 in accordance with 220 C.M.R. § 6.08(2), as in effect from time to time between May 1, 1987 and the date of this Order; and it is

FURTHER ORDERED: That Fitchburg Gas and Electric Light Company shall file within thirty (30) days from the date of this Order a proposal for returning to ratepayers $675,052, plus accumulated interest, over a period not to exceed 139 months, or less if the Company so requests; and it is

FURTHER ORDERED: That Fitchburg Gas and Electric Light Company shall apply an interest rate on the outstanding balance of the $675,052 plus interest accumulated as of the date of this Order calculated in accordance with 220 C.M.R. § 6.08(2); and it is

FURTHER ORDERED: That, Fitchburg Gas and Electric Light Company shall file, on or before July 1, 2001, a new cost of gas adjustment factor in compliance with this Order; and it is

FURTHER ORDERED: That Fitchburg Gas and Electric Light Company shall comply with all other directives contained herein.

By Order of the Department,

_____

James Connelly, Chairman

_____

W. Robert Keating, Commissioner

_____

Paul B. Vasington, Commissioner

_____

Eugene J. Sullivan, Jr., Commissioner

_____

Deirdre K. Manning, Commissioner

Appeal as to matters of law from any final decision, order or ruling of the Commission may be taken to the Supreme Judicial Court by an aggrieved party in interest by the filing of a written petition praying that the Order of the Commission be modified or set aside in whole or in part.

Such petition for appeal shall be filed with the Secretary of the Commission within twenty days after the date of service of the decision, order or ruling of the Commission, or within such further time as the Commission may allow upon request filed prior to the expiration of twenty days after the date of service of the decision, order or ruling. Within ten days after such petition has been filed, the appealing party shall enter the appeal in the Supreme Judicial Court sitting in Suffolk County by filing a copy thereof with the Clerk of said Court. (Sec. 5, Chapter 25, G.L. Ter. Ed., as most recently amended by Chapter 485 of the Acts of 1971).

1. During the D.T.E. 98-51 proceedings, the Company amended its cost of service study to exclude IFCs from base rates (Tr. 5, at 560-561).

2. In 1986 and 1987, the Department amended its CGAC regulations, codified in 220 C.M.R. § 6.00, to allow gas utilities to adjust their rates for firm gas sales on a

semi-annual basis. Cost of Gas Adjustment Clause Rulemaking, D.T.E. 1669-A (1986), 1669-B (1987), 1669-C (1987). Pursuant to the new CGAC regulations, companies were required to use a financing vehicle or trust to finance inventory charges. 220 C.M.R. § 6.06.

3. On March 15, 1999, Fitchburg filed a request for an exception from the requirements of 220 C.M.R. § 6.06. Finding that it was in the public interest, the Department approved the Company's request to finance its gas inventory costs through cash and short-term borrowings pursuant to a cash-pooling agreement. Fitchburg Gas and Electric Light Company, D.T.E. 99-32, at 7 (1999).

4. The Department's questioning concerned Mr. Newhard's recollection of the settlement discussions in D.P.U. 84-145 and whether certain items were included in the Company's rate base.

5. The parties may, in the alternative, employ a mediator, qualified under G.L. c. 233,

§ 23C, in order to raise a claim of statutory privilege that may meet the requirements of G.L. c. 30A, § 11(2).

6. The Department stated in D.P.U. 88-67 that, "If such a motion is granted, however, the exclusion would be limited, as it is in the judicial arena, to admissions of the party making a compromise offer as to the validity of another party's claim in the proceeding." Id. at 25.

7. The Company maintains that the silent inclusion of IFCs in rate base as part of its initial filing in D.T.E. 98-51 was only as a "placeholder" for its COSS (Tr. 5, at 553-555). Fitchburg maintains, in part, that it included the IFCs in the COSS in order to present a complete depiction of what the delivery and supply charges were during the test year (Tr. 5, at 554). Given that Fitchburg's base rate revenue requirement calculations used in D.P.U. 98-51 included $650,076 of gas inventories in rate base (D.P.U. 98-51, at 16, 20), the Department finds the Company's rationale unpersuasive.

8. Since the promulgation of the present version of 220 C.M.R. § 6.00, other LDCs have moved their purchased gas financing costs out of base rates and into the CGAC. See, e.g., Fall River Gas Company, D.P.U. 91-61, at 3 (1991); Commonwealth Gas Company, D.P.U. 91-60, at 2 (1991); Berkshire Gas Company, D.P.U. 90-121, at 234-237 (1990). The Department has reviewed the CGAC tariffs and filings of each LDC, including those of Blackstone Gas Company and North Attleboro Gas Company, for the period 1987 through 1992, and concludes that no other LDC had been collecting IFCs concurrently through both base rates and the CGAC.

9. The Department previously has cautioned the Company about the need to familiarize itself with Department precedent to ensure that its filings are consistent with the principles adopted by the Department. D.T.E. 98-51, at 6, n.3.

10. The Department's approval of the Company's use of its cash-pooling agreement to finance its IFCs was predicated on a finding that the cash-pooling agreement provided the most cost-efficient option for the Company and its ratepayers. D.P.U. 99-32, at 7.

11. The Department acknowledges that any retroactive reduction in the Company's base rates established in D.P.U. 84-145 to compensate for an over-collection could raise issues of retroactive ratemaking. See Fryer v. Department of Public Utilities, 374 Mass. at 689-690; Metropolitan Dist. Commission v. Department of Public Utilities, 352 Mass. at 27-28.

12. In reaching this determination, the Department makes no findings on either the method used by the Company to derive a gas-related return on common equity, or the merits of the ongoing earnings investigation of Fitchburg's electric operations, commenced pursuant to G.L. c. 164, § 93 and docketed as D.T.E. 99-118.